INDEX

CITATIONS

654028—45

In the Supreme Court of the United States

OCTOBER TERM, 1945

No. 119

NEWCOMB CLEVELAND AND BANKERS TRUST COMPANY, AS EXECUTORS OF THE LAST WILL AND TESTAMENT OF ALFRED W. ERICKSON, DECEASED, PETITIONERS

v.

JOSEPH T. HIGGINS, COLLECTOR OF INTERNAL REVENUE FOR THE THIRD DISTRICT OF NEW YORK

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

OPINIONS BELOW

The opinion of the Circuit Court of Appeals (R. 80–84) is reported at 148 F. 2d 722. The first opinion of the District Court (R. 18–28) is reported at 50 F. Supp. 188. The second opinion of the District Court (R. 68–73) is not reported.

JURISDICTION

The judgment of the Circuit Court of Appeals (R. 85) was entered on April 26, 1945. The peti-

tion for a writ of certiorari was filed on June 8, 1945. The jurisdiction of this Court is invoked under Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTION PRESENTED

Whether the court below erred in holding that the petitioners are precluded from maintaining this action for recovery of an amount paid as federal estate tax by reason of the fact that petitioners brought an earlier action, based on an earlier refund claim and on a different ground, for refund of a part of the total estate tax paid, which action, after administrative settlement of the estate tax liability, was dismissed with prejudice upon agreement of the parties.

STATUTE AND REGULATIONS INVOLVED

Revenue Act of 1926, c. 27, 44 Stat. 9:

> SEC. 303 [as amended by Section 805 of the Revenue Act of 1932, c. 209, 47 Stat. 169]. For the purpose of the tax the value of the net estate shall be determined—
>
> (a) In the case of a resident, by deducting from the value of the gross estate—
>
> (1) Such amounts—
>
> * * * * *
>
> (B) for administration expenses,
>
> * * * * *
>
> as are allowed by the laws of the jurisdiction, whether within or without the United States, under which the estate is being administered, * * *.

Treasury Regulations 80 (1934 Ed.):

> ART. 34. ATTORNEY'S FEES.—The executor or administrator, in filing the return, may deduct such an amount as attorney's fees as has actually been paid or which at that time it is reasonably expected will be paid. If on the final audit of a return the fees claimed have not been awarded by the proper court and paid, the deduction will be allowed, provided the Commissioner is reasonably satisfied that the amount claimed will be paid and that it does not exceed a reasonable remuneration for the services rendered, taking into account the size and character of the estate and the local law and practice. If the attorney's fees have not been paid at the time of the final audit of the return the Commissioner may disallow such part, or all, of the deduction as the circumstances may warrant, subject to such future adjustment as the facts may require.
>
> Attorney's fees incident to litigation instituted by the beneficiaries as to their respective interests do not constitute a proper deduction, inasmuch as expenses of this character are properly charges against the beneficiaries personally and are not administration expenses as contemplated by the statute.

STATEMENT

Petitioners are the duly qualified and acting executors of the last will and testament of Alfred W. Erickson, deceased, who died testate, a

resident of the State of New York, on November 2, 1936 (R. 30). As such, they duly filed with the respondent, Collector of Internal Revenue for the Third District of New York, a federal estate tax return for the estate of Alfred W. Erickson, deceased. Acting upon advice of counsel, in filing such return, they exercised the option granted by Section 302 (j) of the Revenue Act of 1926, as amended by Section 404 of the Revenue Act of 1934, and Section 202 (a) of the Revenue Act of 1935, to have the value of all of the property in the estate at the date of death determined for purposes of the tax as of one year after the date of death. (R. 31, 38–39, 41–42.) Also acting on advice of counsel, petitioners failed to include in the gross estate the amount of $242,050.93, representing income of the estate for the period from the date of death to the valuation date as required by Article 11 of Treasury Regulations 80 (1937 Ed.). (R. 31, 38–39, 41–42.)

Upon audit of the decedent's estate tax return, the Commissioner, pursuant to Article 11 of Treasury Regulations 80 (1937 Ed.), included in the gross estate the sum of $242,050.93, representing property which this Court later held in *Maass v. Higgins,* 312 U. S. 443, was not properly includible in the gross estate. As a result, the Commissioner collected a large additional estate tax, plus interest, which included a total of $111,244.40 additional tax and interest resulting from the

erroneous inclusion of this $242,050.93 in the gross estate. (R. 32–34.)

The total estate tax liability as determined by the Commissioner was $1,489,824.71. Petitioners paid the sum of $1,356,653.98 on account of such tax on or about February 1, 1938, and on or about September 29, 1939, they paid the balance of $133,170.73, together with interest amounting to $13,250.48. (R. 32.)

On or about October 24, 1939, petitioners filed a claim for refund of $101,177.27 estate tax and interest (R. 33, 53–58), and on or about November 24, 1939, they filed an amended claim for the same amount (R. 33, 58–63). Both the original and the amended claims were based on the ground that the Commissioner had erroneously included the above $242,050.93 of income of the estate for the year following decedent's death. The amended claim added an alternative demand (R. 63, paragraph (7)), for refund of $51,129.39 on the ground that if the above income of $242,050.93 was properly includible in the gross estate, the value of the gross estate should be reduced by $122,319.12 paid as federal income tax and New York State income tax on the income in question. No other ground for refund was advanced in these claims.

The above refund claims were rejected by the Commissioner on January 29, 1940 (R. 34, 64–66), and on January 19, 1942, petitioners brought an action in the District Court for the Southern Dis-

trict of New York against the respondent, based upon the above claims for refund, to recover the sum of $111,244.40 additional estate tax and interest, together with interest thereon from date of payment (R. 34, 39, 47–52). In the meantime, this Court had decided *Maass* v. *Higgins, supra,* on March 3, 1941. Although administrative settlement was under consideration, this suit was brought for the reason that the statute of limitations was about to toll on petitioners' claim (R. 46).

Following the filing of the above suit on January 19, 1942, certain further negotiations were conducted by counsel for the petitioners with the Commissioner; these culminated in a stipulation for refund of $122,243.53, including interest, and for dismissal of petitioners' complaint. The refund was made to petitioners on or about July 14, 1942, and the complaint in the District Court was dismissed with prejudice. (R. 34, 38–40, 46.)

Following the conclusion of the above litigation, petitioners' attorneys, under date of August 1, 1942, submitted their bill for $18,346.18 for disbursements and services rendered in connection with decedent's estate tax matters. This bill was paid on or about August 21, 1942. (R. 34, 37.)

The record shows that petitioners' attorneys (Phillips & Avery) first began preliminary work on estate tax problems in connection with decedent's estate on December 10, 1936, shortly after his death (R. 38). There is nothing to

show that any compensation had been paid to them prior to the payment of $18,346.18 on August 21, 1942. The contrary is apparent from the contents of their bill for services (R. 37), and it appears from the affidavit of one of the attorneys (R. 38–40) and the affidavit of a trust officer of Bankers Trust Company (R. 41–45) that the greater part of such services had been performed prior to the filing of the complaint on January 19, 1942.

On or about September 14, 1942, shortly after payment of the $18,346.18 for attorney fees on August 21, 1942, petitioners filed a new claim for refund of $7,668.69 on the ground that the attorney fees and expenses of $18,346.18 should be allowed as a deduction from the gross estate as an administration expense under Section 303 (a) of the Revenue Act of 1926, as amended (R. 10–12, 34). The Commissoner rejected this claim on the ground that the question of decedent's estate tax liability was *res judicata* by reason of the final judgment entered in the first suit (R. 13–14, 35). Thereupon, petitioners brought the present action in the District Court for the Southern District of New York, based upon the refund claim filed on September 14, 1942, to recover the sum of $7,668.69, with interest (R. 2–9). The Collector moved to dismiss the complaint on the ground that it failed to state a claim upon which relief could be granted (R. 17). The motion to dismiss

was denied by the District Court on May 20, 1943 (R. 29), pursuant to an opinion by the court (R. 18–28) in which it was held that the question presented by the complaint was not *res judicata*. An answer was filed (R. 15–16), and, on the basis of stipulated facts (R. 30–67), the District Court, after delivering an opinion (R. 68–73), gave judgment for petitioners as prayed (R. 76). The Circuit Court of Appeals reversed the judgment of the District Court and ordered the complaint dismissed (R. 85).

ARGUMENT

The judgment of dismissal with prejudice entered by the District Court in the first suit brought by these petitioners was as conclusive as if it had been entered on the merits after trial. The substance of petitioners' argument in this case is that the prior judgment cannot preclude recovery in this case because the present action is based upon a new claim "which had no existence at any stage of said Action No. 1." (Br. 26.) The record shows, however, that this description of the factual basis for recovery is not an accurate one. The court below properly held that the deduction could and should have been taken into consideration in the final determination of the estate tax liability before the first suit was settled.

It is first urged (Br. 18–25) that the decision below interprets Article 34 of Treasury Regulations 80 (1934 Ed.) in a manner not warranted

by its language or its purpose. The argument is fortified by the assertion that (Br. 27)—

> the Petitioners at the time of said dismissal owed no attorneys' fees and these fees only came into existence as a claim against Petitioners subsequent to the dismissal of said Action No. 1, * * *.

But the court below did not misinterpret the Regulations and the record does not justify the statement that no attorney fees were owed at the time the first action was dismissed.

The first part of Article 34 of Treasury Regulations 80 (1934 Ed.) deals with the deduction of attorney fees at the time of filing the estate tax return, and the court below said that the Regulations do not, in terms, apply to the present situation because they do not expressly apply to claims for refund (R. 83). However, the court correctly pointed out that the Regulations do provide for deduction of prospective attorney fees which the executors will incur and have to pay in administering the estate. Furthermore, the Regulations specifically provide for allowance or disallowance by the Commissioner, "subject to such future adjustment as the facts may require." Both the language and the spirit of the Regulations contemplate the deduction of a reasonable allowance for attorney fees—even if not yet allowed and paid—in the final determination of estate tax liability.

The record shows that the attorneys began per-

forming services in connection with the estate tax matters in December 1936, about two months after decedent's death (R. 38–39). Such services presumably were completed in 1942 when the Government agreed to refund the amount of taxes involved in the first suit. The record does not show what compensation arrangement had been agreed upon by the parties, or whether the $18,346.18, paid in August 1942, was compensation for all services rendered in connection with the decedent's estate tax matters. But the record certainly warrants an inference that this payment represented compensation for all services rendered, and also that most of such services were rendered prior to the filing of the first suit in January 1942. That the attorneys expected, and were entitled to, reasonable compensation for their services must also be assumed even if petitioners did fail to prove the nature of their compensation arrangement.

Finally, the court below properly held that petitioners could and should have claimed the benefit of the deduction here involved, at least by way of estimate, in their first suit. They were under no compulsion to dismiss their first action with prejudice unless they were satisfied with the administrative determination of decedent's estate tax liability. The petitioners made no attempt to raise the question of attorney fees prior to the dismissal of the prior action or to reach any agreement with the Commissioner as to the allowance of the fees.

Moreover, if it should be assumed, contrary to what is the clear import of the Regulations, that the Commissioner would not at any time have allowed a deduction for attorney fees without a claim raising the issue, it should be noted that the *Maass* case was decided in March 1941, and a new, timely, claim could have been filed in time to raise the issue of attorney fees in the prior case. If the fees depended on the amount of recovery, an accurate approximation of the amount due could have been readily made, since administrative settlement was contemplated shortly and the suit was filed only to toll the statute of limitations. The decision in *First Nat. Bank of Birmingham* v. *United States,* 25 F. Supp. 816 (N. D. Ala.) is distinguishable. The decision in that case appears to be based upon the ground that the refund claim was itself inadequate because no amount was specified. Compare *Smith* v. *United States,* 16 F. Supp. 397 (D. Mass.), affirmed without consideration of this point *sub. nom. United States* v. *Nichols,* 92 F. 2d 704 (C. C. A. 1st).

Although the decision below may result in denying a deduction to this estate to which it might be entitled, that is due to the fact that petitioners misconceived their remedy.[1] It must be borne in

[1] Insofar as the issue here involved can be generalized, it has been fairly resolved to allow recovery based on deductions for attorneys' fees even before the amount of the fee is definitely ascertained. See 3 P-H Tax Service (1945) pars. 23,981-23,990. There is no warrant for judicial interference with this generally satisfactory procedure.

mind that the estate tax liability is to be determined as a unit, regardless of the number of issues respecting that liability which might arise. Cf. *Guettel* v. *United States,* 95 F. 2d 229 (C. C. A. 8th), certiorari denied, 305 U. S. 603. If petitioners were right, litigation could be carried on indefinitely were it not for the statute of limitations. Upon termination of the present litigation a new claim for refund could be filed, and a new suit brought, based upon the deductibility of attorney fees paid in connection with this case. The process could be repeated indefinitely. We submit that no such result ever was intended and that the Commissioner's Regulations adequately provide for the situation.

What has been said sufficiently shows that the decision below is not in conflict with any of the decisions relied upon by petitioners (Pet. 8–9) because of the unique factual situation here involved.

CONCLUSION

The decision below is correct and there is no conflict of decisions. Furthermore, because of the peculiar facts of this case, the question involved is not of sufficient general importance to justify review by this Court. The petition for a writ of certiorari should, therefore, be denied.

Respectfully submitted.

HUGH B. COX,
Acting Solicitor General.
SAMUEL O. CLARK, JR.,
Assistant Attorney General.
SEWALL KEY,
HELEN R. CARLOSS,
FRED E. YOUNGMAN,
Special Assistants to the Attorney General.

JULY 1945.

U. S. GOVERNMENT PRINTING OFFICE: 1945